

**Additional Action Is Needed to Eliminate  
Illegal Tax Protester Designations**

**September 2000**

**Reference Number: 2000-10-119**

**This report has cleared the Treasury Inspector General for Tax Administration disclosure review process and information determined to be restricted from public release has been redacted from this document.**



DEPARTMENT OF THE TREASURY  
WASHINGTON, D.C. 20220

INSPECTOR GENERAL  
for TAX  
ADMINISTRATION

September 20, 2000

MEMORANDUM FOR COMMISSIONER ROSSOTTI

A handwritten signature in black ink, reading "Pamela J. Gardiner".

FROM: Pamela J. Gardiner  
Deputy Inspector General for Audit

SUBJECT: Final Audit Report - Additional Action Is Needed to Eliminate  
Illegal Tax Protester Designations

This report presents the results of our annual statutory review to evaluate the Internal Revenue Service's (IRS) compliance with the prohibition to use the Illegal Tax Protester (ITP) or any similar designation. In summary, we found that although IRS management took actions to prevent ITP designations, some actions were not properly performed. As a result, there were still instances when the ITP designation was used after the enactment of the IRS Restructuring and Reform Act of 1998 (RRA 98).<sup>1</sup>

We recommended that the IRS complete its initiatives to remove ITP and similar designations from all areas of operations, including applicable IRS databases, taxpayer cases, training courses, and other documents. Our recommendations will benefit tax administration by protecting taxpayers' rights and improving the reliability of IRS data. Appendix IV of this report provides a detailed description of these benefits, which will be included in our Semiannual Report to the Congress.

Management's response was due on September 8, 2000. As of September 15, 2000, management had not responded to the draft report.

Copies of this report are also being sent to the IRS managers who are affected by the report recommendations. Please contact me at (202) 622-6510 if you have questions, or your staff may call Maurice S. Moody, Associate Inspector General for Audit, (Headquarters Operations and Exempt Organizations Programs), at (202) 622-8500.

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685.

**Additional Action Is Needed to Eliminate  
Illegal Tax Protester Designations**

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**Table of Contents**

Executive Summary.....	Page i
Objective and Scope.....	Page 1
Background .....	Page 2
Results .....	Page 4
The Illegal Tax Protester Designation Was Properly Removed and Controls Were Implemented to Prevent Its Use on the Masterfile .....	Page 5
Case Files and Computer Systems Still Contain References to Illegal Tax Protesters That Were Made After the Effective Date of the Prohibition.....	Page 6
Publications That Made References to Illegal Tax Protesters Were Not Revised or Labeled Obsolete.....	Page 9
New Programs Will Focus on Employee Safety and Taxpayers Using Frivolous Arguments to Avoid Tax Compliance.....	Page 12
Conclusion.....	Page 14
Appendix I – Detailed Objective, Scope, and Methodology .....	Page 16
Appendix II – Major Contributors to This Report.....	Page 20
Appendix III – Report Distribution List.....	Page 21
Appendix IV – Outcome Measures.....	Page 22

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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### **Executive Summary**

The Internal Revenue Service (IRS) Restructuring and Reform Act of 1998 (RRA 98)<sup>1</sup> requires the IRS to stop designating taxpayers as Illegal Tax Protesters (ITP) or any similar designation. This ITP designation was used previously by the IRS to identify individuals and businesses using methods that were not legally valid to protest the tax laws. The Congress was concerned that some taxpayers were permanently labeled and stigmatized by this designation.

Since the ITP designation was recorded on the IRS Masterfile<sup>2</sup> and often became a permanent mark on the taxpayer's record, the RRA 98 specifically required the removal of all existing ITP designations from the IRS' Individual Masterfile. In addition, the RRA 98 stated that the IRS should disregard any such designation not located in the Individual Masterfile.

The United States Code requires the Treasury Inspector General for Tax Administration (TIGTA) to annually evaluate the IRS' compliance with the prohibition to use the ITP or any similar designation.<sup>3</sup> The objective of this audit was to determine if the IRS complied with the provisions of RRA 98 § 3707 and internal IRS guidelines to not designate taxpayers as an ITP or any similar designation. The TIGTA completed its first review of this provision during Fiscal Year (FY) 1999.<sup>4</sup> In that prior review, we conducted limited testing of the IRS Masterfile, internal documents, employee case files, and local inventory systems to determine whether ITP designations were still being used. In our FY 2000 review, we have expanded testing in each of these areas to better determine the IRS' compliance with the law nationwide.

### **Results**

Since the effective date of the RRA 98, the IRS has taken several actions to comply with the prohibition on the use of the ITP designation. Examination Division management requested a computer programming change to remove and prevent the ITP designation from posting on the IRS' Individual Masterfile. Management in different IRS functions issued employee directives to discontinue, remove, or disregard ITP references within

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685.

<sup>2</sup> The IRS database that stores various types of taxpayer account information, which includes data for individuals and businesses.

<sup>3</sup> 26 U.S.C. § 7803(d) (1998).

<sup>4</sup> *The Internal Revenue Service Is Addressing the Use of the Illegal Tax Protestor and Nonfiler Designations*, (Reference Number 199910080, dated September 1999).

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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computer systems, case files, operating manuals, and other publications. In addition, heads of offices were required to review all applicable IRS databases, taxpayer cases, training courses, and other documents by June 1999 to certify whether any ITP references existed. The national ITP certification reported no significant issues with respect to ITP references or coding in computer case inventory systems, manuals, other publications, or case files. However, we did identify ITP designations that violated the RRA 98 in several of these areas.

Although IRS management took actions designed to prevent ITP designations, some actions were not properly performed. The IRS was not always in compliance with the RRA 98 or its internal guidelines because ITP designations and references were still used.

The IRS has established two new programs that were previously components of the ITP Program. The Employee Protection System will focus on employee safety, and the Frivolous Return Program will address taxpayers who use frivolous arguments to avoid tax compliance. These programs are still in the development stage and were not fully operational at the time of our review.

### **The Illegal Tax Protester Designation Was Properly Removed and Controls Were Implemented to Prevent Its Use on the Masterfile**

As required by the RRA 98, the IRS removed the ITP designation from its Individual Masterfile in January 1999. Using computer extracts of the IRS Masterfile obtained in August 1999 and April 2000, we verified that the ITP designation does not exist on any taxpayer account.

There were approximately 57,000 taxpayer accounts with the ITP designation on the IRS Masterfile before the removal mandated by the RRA 98. Because the RRA 98 also prohibited the IRS from using any designation similar to the ITP, we reviewed these accounts to determine if there was any movement to another Masterfile designation. The prior ITP designation on the Masterfile was one of eight designations used to accelerate enforcement action on tax accounts. We found that there were no reassignments of the 57,000 taxpayers formerly designated as ITPs to any of the other eight Masterfile designations or to the Potentially Dangerous Taxpayer (PDT) Masterfile designation.

### **Case Files and Computer Systems Still Contain References to Illegal Tax Protesters That Were Made After the Effective Date of the Prohibition**

The RRA 98 directed the IRS to no longer designate taxpayers as ITPs and to disregard all previous references to ITPs. While IRS management issued directives to comply with

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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this provision, case files and computer systems still contain references to ITPs made after the effective date of the law.<sup>5</sup>

From a judgmental sample of 974 case files in the Appeals, Collection, Examination, and Taxpayer Advocate offices in 2 service centers and 2 district offices, we found IRS employees made references to ITPs in 96 case files after the effective date of the RRA 98. In addition, based on a national computer extract of the Automated Collection System (ACS), we identified from a statistical sample 89 case histories with ITP references and projected that IRS employees could have made approximately 450 references to ITPs in the ACS case histories. When we asked employees why they still used the term, they generally replied that although they knew about the change in the law, they sometimes inadvertently still followed the old procedures.

Based on national computer extracts taken from November 1999 through January 2000, two case inventory systems did not have ITP designated codes removed as instructed by management. The Taxpayer Advocate Management Information System (TAMIS) contained 176 records with ITP codes that had been input after the effective date of the RRA 98. The ITP code on the TAMIS was redefined to a reserved status in August 1999; however, due to an application problem and outdated procedures, employees still used the code. The Audit Information Management System (AIMS) contained 687 active records with ITP codes, with 83 of these active cases input after the effective date of the RRA 98. Although management made requests to prevent use of the ITP code on the AIMS, they did not monitor the system to ensure compliance.

### **Publications That Made References to Illegal Tax Protesters Were Not Revised or Labeled Obsolete**

After the effective date of the RRA 98, IRS management issued directives to review and update its various publications to eliminate references to ITP terminology and programs. However, the Internal Revenue Manual (IRM) and other IRS publications still contained references to ITPs.

In our FY 1999 annual review, the IRM on an IRS Intranet site contained 50 sub-sections with references to ITPs. Management's corrective action stated that all references would be removed by February 2000. However, as of March 2000, there were still 19 IRM sub-sections with ITP references remaining on the Intranet site. Further research of the IRM on that Intranet site identified an additional 115 sub-sections with references to ITPs. References to ITPs were also found in other IRM versions available to IRS employees. The Examination Division was responsible for IRM updates to remove ITP references for all IRS divisions. However, it was difficult for Examination personnel to obtain approvals from the other divisions for the IRM updates.

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<sup>5</sup> The effective date of RRA 98 § 3707 was July 22, 1998, for all provisions except for the requirement to remove ITP codes from the IRS Masterfile, which was effective January 1, 1999.

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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We also searched the titles of IRS forms, documents, letters, and training materials for ITP references. There were 43 publications with references to ITPs in their titles, of which 15 were available for dissemination to employees. In many cases, employees assigned to update these publications had changed jobs or left the IRS. In addition to the 15 active publications with ITP references in the titles, we identified 4 other publications that contained ITP references not in the titles but in the text of the publications.

### **New Programs Will Focus on Employee Safety and Taxpayers Using Frivolous Arguments to Avoid Tax Compliance**

Congressional committee reports stated that the removal of the ITP designation was not intended to diminish employee safety and provided the IRS with the authority to keep additional records to protect employees. As a result, the IRS developed the Employee Protection System to enhance employee safety when dealing with taxpayers who harass or threaten financial harm to IRS employees. Our review of the program's plans indicates that, if implemented as designed, it should be in conformance with the RRA 98.

The Internal Revenue Code provides for a specific penalty related to frivolous tax returns.<sup>6</sup> The IRS developed the Frivolous Return Program to address taxpayers using frivolous arguments to avoid tax compliance. This program is intended to improve the consistency of taxpayer treatment by centralizing correspondence, education, and tax enforcement actions. It is possible that this new program will be perceived to be similar to the old ITP Program because it can address some of the same taxpayers and compliance issues. However, the IRS' plans are that the new program will address taxpayers who use frivolous arguments to avoid paying taxes. The IRS also plans to implement controls to prevent the use of a permanent label that could stigmatize taxpayers when they become compliant. A future TIGTA review will address this program as it becomes operational.

### **Summary of Recommendations**

We recommend that the IRS complete its initiatives to remove ITP and similar designations from all areas of operation, including applicable IRS databases, taxpayer cases, training courses, and other documents.

Management's Response: Management's response was due on September 8, 2000. As of September 15, 2000, management had not responded to the draft report.

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<sup>6</sup> 26 U.S.C. § 6702 (1982).

## Additional Action Is Needed to Eliminate Illegal Tax Protester Designations

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### Objective and Scope

*The TIGTA is required to annually evaluate the IRS' compliance with not designating taxpayers as Illegal Tax Protesters.*

The United States Code requires the Treasury Inspector General for Tax Administration (TIGTA) to annually evaluate the Internal Revenue Service's (IRS) compliance with the IRS Restructuring and Reform Act of 1998 (RRA 98)<sup>1</sup> § 3707. Specifically, RRA 98 § 3707 prohibits the designation of taxpayers as Illegal Tax Protesters (ITP) or any similar designation. The objective of this audit was to determine if the IRS complied with the provisions of RRA 98 § 3707 and internal IRS guidelines to not designate taxpayers as an ITP or any similar designation. This is our Fiscal Year (FY) 2000 review, with the FY 1999 review<sup>2</sup> being our initial evaluation of the ITP provision.

In that prior review, we conducted limited testing of the IRS Masterfile,<sup>3</sup> internal documents, employee case files, and local inventory systems to determine whether ITP designations were still being used. We also reviewed initial proposals for the IRS' Frivolous Return Program.

In our FY 2000 review, we have expanded testing in each of these areas to better determine the IRS' compliance with the law nationwide. We also reviewed designs for the implementation of the IRS' Employee Protection System to determine whether its design is in compliance with the ITP provisions of the RRA 98.

*Fieldwork occurred between November 1999 and May 2000.*

We conducted our review using information from national IRS databases and performed fieldwork in the Pacific-Northwest and Southwest Districts, as well as the Fresno and Ogden Service Centers. These field sites

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685.

<sup>2</sup> *The Internal Revenue Service Is Addressing the Use of the Illegal Tax Protestor and Nonfiler Designations*, (Reference Number 199910080, dated September 1999).

<sup>3</sup> The IRS database that stores various types of taxpayer account information, which includes data for individuals and businesses.



## Additional Action Is Needed to Eliminate Illegal Tax Protester Designations

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were selected because they had the highest number of taxpayer cases that were formerly classified under the ITP Program. We also performed fieldwork at the Western Area Distribution Center to determine whether active ITP publications were still available. Our review was performed between November 1999 and May 2000 in accordance with *Government Auditing Standards*.

Details of our objective, scope, and methodology are presented in Appendix I. Major contributors to this report are listed in Appendix II.

### Background

Before passage of the RRA 98, the IRS had the ITP Program to identify individuals and businesses using methods that were not legally valid to protest the tax laws. Taxpayers could be referred to the ITP Program if their tax returns or correspondence contained specific indicators of noncompliance with the tax law, including the following examples:

*Before the RRA 98, taxpayers could be referred to the ITP Program if specific noncompliance issues existed.*

- Claims that salaries and wages are not “income” within the meaning of the Sixteenth Amendment.
- Submits a tax return with zero money amounts and claims there is no section of the Internal Revenue Code that establishes an income tax liability.
- Claims not to be a citizen of the United States and has no income from sources within the United States, but rather claims to be a citizen of a “state republic” or that all 50 states are foreign countries.
- Claims not to be a “person” or “individual” within the meaning of the Internal Revenue Code and not subject to income taxes.
- Claims that the Sixteenth Amendment was not properly ratified and the federal government does not have the legal authority to collect an income tax without apportionment.

## Additional Action Is Needed to Eliminate Illegal Tax Protester Designations

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- Refuses to file or pay because they disagree with government policies or spending plans.
- Claims income is not taxable because of the declining value of the dollar.

The IRS district offices had tax protester coordinators who were responsible for determining whether a taxpayer should be included in the ITP Program. If a taxpayer was classified as an ITP, the taxpayer's record was coded as such on the IRS' main computer system, called the Masterfile. The Masterfile includes both individual and business taxpayer accounts. Once a taxpayer's account was coded, certain types of tax law enforcement actions, such as collection efforts, were accelerated. The designation was also intended to notify IRS employees to be cautious so that they would not be drawn into confrontations with these taxpayers.

*The Congress was concerned that taxpayers were stigmatized by the ITP designation.*

Concerns were raised by the Congress that some taxpayers were permanently labeled and stigmatized by the ITP designation. Taxpayers who subsequently complied with the tax laws could continue to be labeled as ITPs because of coding on the IRS' main computer system. This ITP designation and computer coding could bias IRS employees and result in unfair treatment.

To address these concerns, the Congress included the following ITP provisions in the RRA 98:

- The officers and employees of the IRS shall not designate taxpayers as illegal tax protesters (or any similar designation).
- The IRS shall remove such designation from the Individual Masterfile by January 1, 1999, and shall disregard any such designation not located in the Individual Masterfile.
- An officer or employee of the IRS may designate any appropriate taxpayer as a nonfiler but shall remove such designation once the taxpayer has filed income tax returns for 2 consecutive taxable years and paid all taxes shown on such returns.

*The RRA 98 prohibited designating taxpayers as ITPs but allowed the nonfiler designation and the ability to ensure employee safety.*

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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A Conference Committee agreement for the RRA 98 also allows the IRS to implement additional procedures such as the maintenance of appropriate records, if needed to ensure IRS employees' safety.

### **Results**

Since the effective date of the RRA 98, IRS management has taken several actions to comply with the prohibition on the use of the ITP designation. Examination Division management requested a computer programming change to remove and prevent the ITP designation from posting on the IRS' Masterfile. In addition, management issued directives to the different tax enforcement functions to discontinue, remove, or disregard ITP references within computer systems, case files, operation manuals, training materials, and other publications.

*Despite the IRS' actions, including the national ITP certification that reported no violations, ITP references were still included in taxpayer cases, computer systems, documents, and procedures.*

To help ensure that all appropriate actions were taken to eliminate this designation, the Chief Operations Officer required heads of offices to certify by June 1999 if any ITP references existed. This national ITP certification was sent to all National Offices, service centers, and district offices. The certification covered all applicable IRS databases, taxpayer cases, training courses, and other documents. The national ITP certification reported no significant issues with respect to ITP references or coding in computer case inventory systems, manuals, other publications, or case files.

Despite the IRS' efforts with this certification, ITP references were still included in case files, computer inventory systems, operational manuals, and publications.

The IRS has established two new programs that were previously components of the ITP Program. The Employee Protection System will focus on employee safety, and the Frivolous Return Program will address taxpayers who use frivolous arguments to avoid tax compliance. These programs are still in the

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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development stage and were not fully operational at the time of our review.

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### **The Illegal Tax Protester Designation Was Properly Removed and Controls Were Implemented to Prevent Its Use on the Masterfile**

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*Masterfile computer extracts taken in August 1999 and April 2000 confirmed the ITP designation was not reintroduced.*

In our FY 1999 review, we confirmed that the IRS had removed the ITP designation from the Masterfile in January 1999. In our FY 2000 review, we obtained computer extracts of the individual and business portions of the Masterfile in August 1999 and April 2000 to determine if the ITP designation was reintroduced on the Masterfile. There were no taxpayer accounts with the ITP designation on the Masterfile.

To prevent the reintroduction of the ITP designation, the IRS updated a Masterfile data input computer check to reject requests attempting to establish an ITP designation on a taxpayer's account. In addition, the IRS computer system does not archive ITP designations on retention files; therefore, the ITP designation cannot be reintroduced to the Masterfile when archived taxpayer accounts are called back to the Masterfile.

*No ITP or similar designations were found on the Masterfile.*

There were approximately 57,000 taxpayers designated as ITPs on the IRS Masterfile before the removal required by the RRA 98. Since the RRA 98 also prohibited using any designation similar to the ITP, we checked the 57,000 taxpayer accounts for movement to another Masterfile designation. The prior ITP designation on the Masterfile was one of eight designations used to accelerate enforcement action on tax accounts. There were no reassignments of the 57,000 taxpayers formerly designated as ITPs to any of these other Masterfile designations.

We also reviewed the 57,000 accounts to determine whether they had been reassigned to the Masterfile designation Potentially Dangerous Taxpayer (PDT). The PDT designation is used to identify individuals who

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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have assaulted or threatened bodily harm to IRS employees. There were no reassignments of the 57,000 taxpayers formerly designated as ITPs to the PDT designation.

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### **Case Files and Computer Systems Still Contain References to Illegal Tax Protesters That Were Made After the Effective Date of the Prohibition**

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*Case files and computer systems still contain ITP references that were made after the effective date of the RRA 98.*

The RRA 98 directed the IRS to no longer designate taxpayers as ITPs and to disregard all previous references to ITPs. IRS management issued directives for the actions needed to comply with this provision. Despite these directives and the subsequent certification, case files and computer systems still contained references to ITPs that were made after the effective date of the law.<sup>4</sup> Management did not adequately review the computer files to determine whether these codes were still being used before completing the certification.

#### **IRS employees referred to taxpayers as ITPs in case files**

*From a judgmental sample of case files in various IRS functions, there were 96 case files with ITP references made after the effective date of the RRA 98.*

To determine if IRS employees made references to taxpayers as ITPs, we reviewed case files in the Pacific-Northwest and Southwest Districts, as well as the Fresno and Ogden Service Centers. We reviewed a judgmental sample of 974 Appeals, Collection, Examination, and Taxpayer Advocate office case files for taxpayers identified as ITPs before the passage of RRA 98. IRS employees made ITP references after the effective date of the RRA 98 in 96 of these case files.

*From a statistical sample of ACS case files, we project that 450 ACS files contained ITP references.*

In addition, we extracted from the national Automated Collection System (ACS) case histories with wording that could indicate an ITP reference. From the extract of 1,850 cases, we selected a statistical random sample of 366 cases to review. In the sample, 89 case histories

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<sup>4</sup> The effective date of RRA 98 § 3707 was July 22, 1998, for all provisions except for the requirement to remove ITP codes from the IRS Masterfile, which was effective January 1, 1999.

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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(24.3 percent) contained a reference to ITPs made after the effective date of the RRA 98. Based on this sample, we project that 450 ACS case histories could contain an ITP reference made after the effective date of the RRA 98.

When we asked employees why they still made ITP references, they generally replied that although they knew about the change in the law, they sometimes inadvertently still followed the old procedures.

### **Recommendation**

1. The national heads of office should remind managers and employees within the Appeals, Collection, Customer Service, Examination, and Taxpayer Advocate offices that ITP references are not to be made in IRS case files. Managers should counsel employees who use the ITP reference.

Management's Response: Management's response was due on September 8, 2000. As of September 15, 2000, management had not responded to the draft report.

### **Computer inventory systems contain ITP designation codes**

In addition to the Masterfile, the IRS also uses other computer systems to manage taxpayer case inventories. To ensure compliance with the RRA 98, IRS management issued directives to prohibit the use of ITP coding on these computer inventory systems.

We reviewed national computer extracts from four inventory systems that could have the ITP designation. We obtained extracts from November 1999 through January 2000 to evaluate compliance with the law and management directives. The Appeals Consolidated Database System and the Criminal Investigation Management Information System did not contain ITP codes. However, two inventory systems did contain ITP codes that were used after the effective date of the RRA 98.

*The Taxpayer Advocate and Examination offices still have ITP coding on their computer inventory systems.*

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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*The TAMIS had 176 cases and the AIMS had 83 cases with ITP coding input after the effective date of the RRA 98.*

The Taxpayer Advocate Management Information System (TAMIS) had 176 records with coding previously used for ITPs. All 176 records had been input after the RRA 98 effective date. The ITP coding on the TAMIS was redefined to a reserved status in August 1999. However, employees were still using the ITP coding because of outdated procedure documents and the system could not prevent the input of these codes. The TAMIS programming cannot be updated until an Informix application problem is first resolved. Once the application problem is fixed, there are plans to update the TAMIS coding to include removal of the ability to use the ITP coding.

The Audit Information Management System (AIMS) had 687 active records with ITP codes. Of these, 83 cases were input after the RRA 98 effective date. The same ITP coding on the AIMS can also be found on its associated system called the Examination Returns Control System. To prevent ITP coding on the AIMS, Examination management submitted a request for Information Systems to create a computer validity check for the input of ITP codes on the AIMS. Management subsequently decided that the input validity check was no longer necessary because the AIMS has a validity check for summary reports that disregards invalid codes, including ITP codes. In addition, management directed employees not to use ITP coding on the AIMS.

However, management did not monitor the system to ensure employee compliance, which indicates that the input validity check is still needed. If a computer validity check for input codes is added, then the validity check for summary reports may not be necessary.

### **Recommendations**

2. The Assistant Commissioner (Examination) and the National Taxpayer Advocate should review and remove any remaining ITP coding from active taxpayer files within the AIMS and the TAMIS.
3. The National Taxpayer Advocate and the Chief Information Officer should expedite the resolution of

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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the Informix application problem in order for TAMIS programming to be updated.

4. The Assistant Commissioner (Examination), in coordination with the Director for Systems Development, should implement a computer validity check to the AIMS that will prevent the input of ITP coding.

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### **Publications That Made References to Illegal Tax Protesters Were Not Revised or Labeled Obsolete**

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*The IRM and other publications still contained ITP designations that could be used or followed by employees.*

After the effective date of the RRA 98, IRS management issued directives to review and update its various publications to eliminate references to ITP terminology and programs. In addition, a national ITP certification requested that all operational manuals, including the Internal Revenue Manual (IRM), be thoroughly reviewed and updated to eliminate references to ITP terminology and programs by the end of June 1999. In response to our FY 1999 review, IRS management stated that ITP references in the IRM would be removed.

Although some of the ITP references were removed, these directives were not properly completed, and the IRM and other publications still contained ITP references and guidelines that could be used or followed by employees. The IRS' national ITP certification did not identify these uncorrected ITP references.

#### **Operational manuals still contain ITP references**

*The IRM on an IRS Intranet site contained at least 134 ITP references.*

Our review in FY 1999 identified 50 IRM sub-sections containing references to ITPs on an IRS Intranet site called the Compliance Automated Research Tool System (CARTS). Management responded that the ITP references on the IRM Intranet site would be removed by February 1, 2000. However, as of March 2000, the IRS Intranet site still contained 19 of the 50 previously identified sub-subsections with ITP references.



## Additional Action Is Needed to Eliminate Illegal Tax Protester Designations

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Further research of the IRM on the IRS CARTS Intranet site found 115 additional sub-sections with ITP references. Each division is responsible for updating its own section of the IRM to ensure removal of these references. The following table shows the ITP references that we identified in our research by IRM section.

**Table I - ITP References Still in the IRM**

IRM Section	Sub-sections with Uncorrected References	Additional Sub-sections with References	Totals
Administration	5	11	16
Chief Counsel	3	17	20
Collection	2	17	19
Criminal Investigation	-	9	9
Employee Plans	1	7	8
Examination	6	36	42
Inspection	1	9	10
Personnel	-	8	8
(Multifunctional)	1	1	2
<b>Totals</b>	<b>19</b>	<b>115</b>	<b>134</b>

*ITP references were found on different IRM Intranet sites and in printed format.*

The IRM is published on different media, including paper format, various Intranet sites, and CD-ROM. We identified ITP references in each media type. Many of the IRM sections were revised in January 2000 but still contained the ITP references.

Although each division is responsible for its own IRM section, in our FY 1999 review, IRS management appointed the Assistant Commissioner (Examination Division) to ensure the IRM was updated for all IRS divisions. Some difficulty was encountered by Examination personnel in obtaining the necessary approvals from the other divisions for the IRM updates.

## Additional Action Is Needed to Eliminate Illegal Tax Protester Designations

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### Recommendation

5. Each IRS division should review its operational manuals for ITP references. These references should be removed upon the next revision of the manuals.

### Publications contain ITP references

*Employees had access to 15 publications with ITP references in the titles.*

Using the IRS' Electronic Publishing Intranet site, we searched the titles of IRS forms, documents, letters, and training materials for ITP references. There were 43 publications with references to ITPs in their titles. Of these 43 publications, 15 used the term improperly and were available for dissemination to employees. IRS records indicate that employees had ordered 10 of these 15 publications after the effective date of the RRA 98. The following table shows the 15 publications with ITP references in the title that we identified in our research, by originator of the publication.

**Table II - ITP References in Publication Titles**

Originator of the Publication	Publications with ITP References
Collection	1
Criminal Investigation	2
Examination	4
Inspection	1
Training	5
Unknown Originator	2
<b>Totals</b>	<b>15</b>

During office reviews at two service centers and two district offices, we identified four other publications that contained ITP references in the text of the publications rather than in the titles. It was not feasible to search the text of every IRS publication, so there may be other publications with ITP references contained in the text.

IRS management issued directives to review its publications for ITP references. However, these IRS publications were not adequately reviewed before

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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*Some employees assigned to update publications no longer have this responsibility or have left the IRS.*

management certified that publications did not contain ITP references.

IRS guidelines require a review of publications every 2 years to determine whether publications should be revised or labeled obsolete. Of the 15 publications with ITP references, none of the publications were revised within the last 2 years. In many cases, the specific employees (publishing analysts and originators) assigned to update these publications no longer have this responsibility or no longer work for the IRS.

### **Recommendations**

6. The Assistant Commissioner (Forms and Submission Processing), with the assistance of the appropriate division, should ensure current employees (publishing analysts and originators) are assigned to review the publications within the 2-year review period, as stated in their guidelines.
7. The appropriate originator, in coordination with the Assistant Commissioner (Forms and Submission Processing), should revise or label as obsolete the 15 publications that we identified with ITP references.

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### **New Programs Will Focus on Employee Safety and Taxpayers Using Frivolous Arguments to Avoid Tax Compliance**

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After the effective date of the RRA 98, the IRS started developing two new programs to promote employee safety and address tax compliance which had previously been components of the ITP Program.

These new programs are the Employee Protection System and the Frivolous Return Program. Both programs are in their development stage and plan to have controls to help ensure compliance with the RRA 98.

## Additional Action Is Needed to Eliminate Illegal Tax Protester Designations

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*The Employee Protection System will incorporate the PDT system and harassment indicators.*

### **The Employee Protection System is designed to enhance employee safety**

Congressional committee reports stated that the removal of the ITP designation was not intended to diminish employee safety and provided the IRS with the authority to keep additional records to protect employees.

Although the IRS already had the PDT Program, which provided a designation to address taxpayers who physically assault or threaten bodily harm to IRS employees, it created the Employee Protection System to enhance employee safety. The Director of the Michigan District is the executive in charge of the design for this program.

This program will provide IRS employees the ability to identify taxpayers who have harassed or threatened financial harm to IRS employees. The IRS plans to include the PDT program as a component of the Employee Protection System. Although the IRS has not yet finalized the design of this program, our review of the plans for this program indicates that if it is implemented as designed, it should be in conformance with the RRA 98.

### **The Frivolous Return Program is designed to address taxpayers using frivolous arguments to avoid tax compliance**

*The IRS determined that it must still address taxpayers who purposely make arguments that are not legally valid to avoid the payment of taxes.*

Although the RRA 98 directs the IRS to not designate taxpayers as ITPs, the IRS determined that it must still address individuals and businesses who do not comply with the law by purposely making arguments that are not legally valid to avoid the payment of taxes. The IRS created the Frivolous Return Program to address this tax compliance issue. The Director of the Rocky Mountain District is the executive in charge of the design for this program.

The Internal Revenue Code provides for a specific penalty related to frivolous tax returns.<sup>5</sup> The foundation

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<sup>5</sup> 26 U.S.C. § 6702 (1982).

## Additional Action Is Needed to Eliminate Illegal Tax Protester Designations

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*The Frivolous Return  
Program plans to address  
taxpayer behavior without  
stigmatizing the taxpayer.*

of this program is to improve the consistency of taxpayer treatment by centralizing correspondence, education, and tax enforcement actions.

The plans for this program include the use of transaction codes to identify taxpayers who file invalid, frivolous tax returns or send frivolous correspondence and have not complied with filing requirements. These codes will be used to assist in compliance efforts and to initiate educational outreach. Compliance efforts will include reviews to determine whether the taxpayer has met filing and payment requirements. Educational outreach will include sending correspondence to the taxpayers addressing the legal precedents and the ramifications of using their specific arguments to avoid complying with the tax law.

It is possible that this new program will be perceived to be similar to the old ITP Program because it can address some of the same taxpayers and compliance issues. However, the IRS' plans are that the new program will address taxpayers who use frivolous arguments to avoid paying taxes. The IRS also plans to institute controls that ensure codes will be reversed for taxpayers who are compliant with the tax law for 2 consecutive years. This should prevent the use of a permanent label that could stigmatize taxpayers after they become compliant. A future TIGTA review will address this program as it becomes operational.

### Conclusion

While the IRS has taken certain actions to comply with the prohibition of the ITP designation, additional actions are needed to eliminate the use of this designation. These actions include the following:

*The IRS should complete its  
initiatives to remove ITP  
references and emphasize  
monitoring these actions to  
ensure compliance with the  
RRA 98.*

- Ensure employees remain aware that they should not refer to taxpayers as ITPs.
- Remove and prevent ITP coding on the AIMS and TAMIS computer inventory systems.

### **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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- Remove ITP references from operational manuals, including the IRM.
- Remove ITP references from publications or label the ITP publications obsolete and ensure publications are reviewed within the required 2-year internal review period.

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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### **Appendix I**

#### **Detailed Objective, Scope, and Methodology**

The objective of this audit was to determine if the Internal Revenue Service (IRS) complied with the provisions of the IRS Restructuring and Reform Act of 1998 (RRA 98)<sup>1</sup> § 3707 and internal IRS guidelines to not designate taxpayers as Illegal Tax Protesters (ITP) or any similar designation. To achieve this objective, we performed the following tests:

- I. To determine if the ITP designation is currently being used on the IRS Masterfile<sup>2</sup> and if taxpayers who were previously identified as ITPs were reclassified to a different Masterfile designation, we:
  - A. Reviewed Masterfile program documents and interviewed Information Systems employees to identify computer validity checks designed to prevent the ITP designation from posting to the Masterfile.
  - B. Obtained an August 1999 and April 2000 Masterfile computer extract of all taxpayers with an accelerated enforcement action designation to identify any taxpayer with the ITP designation and determine if any prior ITP designated taxpayers were reclassified to a different code which could accelerate enforcement action.
- II. To determine if prior ITP designated taxpayers on the Masterfile retention registers can be recalled to the active Masterfile with the ITP designation, we reviewed Masterfile program documents and interviewed Information Systems employees to identify information to recall data from the retention registers to the active Masterfile.
- III. To determine if prior ITP designated taxpayers were reclassified to a Potentially Dangerous Taxpayer (PDT) designation, we:
  - A. Reviewed trends in the PDT population before and after the effective date of the RRA 98 using Masterfile computer extracts of all PDT designated taxpayers in December 1998, January 1999, and August 1999.

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685.

<sup>2</sup> The IRS database that stores various types of taxpayer account information, which includes data for individuals and businesses.

### **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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- B. Matched an August 1999 Masterfile computer extract of all taxpayers with a PDT designation to an extract of prior ITP designated taxpayers to determine possible reclassification.
  - C. Tested the internal control of the Integrated Data Retrieval System (IDRS)<sup>3</sup> command code to limit employee access to input the PDT designation on the Masterfile. We obtained an IDRS Audit Trail computer extract of all employees entering the command code from January 1998 to August 1999 and verified the employees' authorization.
- IV. To determine if IRS management directives to remove ITP designations from other major IRS computer systems were accomplished, we:
- A. Obtained between November 1999 and January 2000 computer extracts of the Audit Information Management System (AIMS), the Criminal Investigation Management Information System, the Appeals Consolidated Data System, and the Taxpayer Advocate Management Information System (TAMIS) to identify cases containing coding that refers to ITPs.
  - B. Interviewed employees, management, and Information Systems personnel to determine why taxpayers on the AIMS and the TAMIS were still coded as ITPs.
  - C. Confirmed at the Pacific-Northwest and the Southwest Districts between January 2000 and March 2000 whether the same ITP coding on the AIMS can also be found on its associated system called the Examination Returns Control System.
- V. To determine if IRS employees are using ITP designations or referring to taxpayers as ITPs, we:
- A. Reviewed documentation and interviewed management involved with the IRS' national ITP certification to identify possible ITP issues and any corrective action to remove ITP designations.
  - B. Interviewed managers and the RRA 98 Coordinators at the Ogden and Fresno Service Centers and the Pacific-Northwest and Southwest Districts between January 2000 and March 2000 to determine if employees received training for the RRA 98 changes.
  - C. Reviewed a judgmental sample of 974 of Appeals, Collection, Examination, and Taxpayer Advocate office case files at the Ogden and Fresno Service Centers and the Pacific-Northwest and Southwest Districts between

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<sup>3</sup> The IRS computer system capable of retrieving or updating stored taxpayer account information.



## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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January 2000 and March 2000 to determine if employees made references to taxpayers as ITPs. The cases were selected based on whether the taxpayer was designated as an ITP before the effective date of the RRA 98.

- D. Obtained a November 1999 computer extract of the Automated Collection System (ACS) to identify taxpayer cases with key words including “TXPR,” “ITP,” and “PROTEST” in the history section, and then took a statistical random sample of 366 cases to determine if the employees made an ITP reference. The sample is based on a population of 1,850, confidence level of 95 percent, precision of plus or minus 4 percent, and occurrence rate of 25 percent. Interviewed 18 employees at the Ogden and Fresno Service Centers and the Pacific-Northwest District between January 2000 and March 2000 to determine why ITP references were made on the ACS.
- VI. To determine if IRS operational manuals have been updated to eliminate ITP references, we:
- A. Reviewed an IRS Intranet site called the Compliance Automated Research Tool System (CARTS) in March 2000 for ITP references in the Internal Revenue Manual (IRM). We followed up on the 50 sections identified in our Fiscal Year (FY) 1999 review and searched for any additional references.
  - B. Reviewed a judgmental sample of 10 ITP references in the IRM found on the CARTS Intranet site to determine if these same ITP references were also contained in the IRS Electronic Publishing Intranet site (this site allows IRS employees to obtain electronic and printed versions of the IRM). This was performed in March 2000.
  - C. Reviewed the IRS Intranet site called the Servicewide Electronic Research Project in March 2000 for ITP references in the IRM.
  - D. Interviewed management for why the corrective actions to our FY 1999 report to revise the IRM before February 1, 2000, have not been completed.
- VII. To determine if IRS publications have been updated to eliminate ITP references, we:
- A. Reviewed the publication *ADP and IDRS Information* (Document 6209, revised in January 2000) for ITP references. We followed up on ITP references identified in our FY 1999 review and searched for any additional references.
  - B. Reviewed publications by title for ITP references using the IRS Electronic Publishing Intranet site in September 1999 and the printed copy of *IRS Published Product Catalog* (Document 7130, revised in January 1999).

### **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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(Note: The IRS Electronic Publishing Intranet site shows if the publication has an electronic version available and the current status of the publications.)

- C. For the publications identified with ITP references in the title, we interviewed management and employees at the Western Area Distribution Center to confirm the current status of the publications. We used the Centralized Inventory Distribution System Transaction Report for November 1998 to November 1999 to determine if any of the publications with ITP references in the title were still active.
  - D. For the 15 active publications identified with ITP references in the titles, we interviewed National Office management and employees (publishing analysts and originators) assigned to the publications to determine if they were following IRS guidelines to review publications every 2 years.
  - E. Conducted a general review of publications when conducting other tests at the Ogden and Fresno Service Centers and the Pacific-Northwest District between January 2000 and March 2000.
- VIII. To determine if new IRS programs are following the ITP provisions of the RRA 98, we:
- A. Reviewed the design plan for the Frivolous Return Program and discussed future activity with management and employees.
  - B. Reviewed the design plan for the Employee Protection System and discussed future activity with management and employees.

**Additional Action Is Needed to Eliminate  
Illegal Tax Protester Designations**

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**Appendix II**

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**Additional Action Is Needed to Eliminate  
Illegal Tax Protester Designations**

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**Appendix III**

**Report Distribution List**

Deputy Commissioner Operations C:DO  
Chief Counsel CC  
National Taxpayer Advocate TA  
Chief, Appeals AP  
Chief Information Officer IS  
Chief Operations Officer OP  
Executive Officer for Service Center Operations OP:SC  
Chief, Customer Service Field Operations OP:CSF  
Assistant Commissioner (Collection) OP:CO  
Assistant Commissioner (Customer Service) OP:C  
Assistant Commissioner (Examination) OP:EX  
Assistant Commissioner (Forms and Submission Processing) OP:FS  
Chief, Criminal Investigation CI  
Director, Legislative Affairs CL:LA  
Director, Office of Program Evaluation and Risk Analysis M:O  
Office of Management Controls M:CFO:A:M  
Director, Fresno Customer Service Center  
Director, Ogden Customer Service Center  
Director, Michigan District  
Director, Pacific-Northwest District  
Director, Rocky Mountain District  
Director, Southwest District  
Liaisons:  
    Deputy Commissioner Operations C:DO  
    Chief Counsel CC  
    National Taxpayer Advocate TA  
    Chief, Appeals AP  
    Chief Information Officer IS  
    Chief Operations Officer OP  
    Executive Officer for Service Center Operations OP:SC  
    Chief, Customer Service Field Operations OP:CSF  
    Assistant Commissioner (Collection) OP:CO  
    Assistant Commissioner (Customer Service) OP:C  
    Assistant Commissioner (Examination) OP:EX  
    Assistant Commissioner (Forms and Submission Processing) OP:FS  
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## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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### **Appendix IV**

#### **Outcome Measures**

This appendix presents information on the impact that our recommended corrective actions will have on tax administration. These benefits will be incorporated into our Semiannual Report to the Congress.

##### Finding and recommendation:

Internal Revenue Service (IRS) employees made references to taxpayers as Illegal Tax Protesters (ITP) in Appeals, Collection, Customer Service, Examination, and Taxpayer Advocate office case files (see page 6). This report recommends that management remind employees not to make ITP references and to counsel employees who continue to make ITP references.

##### Type of Outcome Measure:

Taxpayer Rights – Actual and Potential

##### Value of the Benefit:

IRS employees in 4 IRS offices made references to taxpayers as ITPs in 96 Appeals, Collection, Examination, and Taxpayer Advocate office case files after the effective date of the IRS Restructuring and Reform Act of 1998 (RRA 98).<sup>1</sup> In addition, nationwide, employees using the Automated Collection System (ACS) made approximately 450 references to taxpayers as ITPs in case files.

##### Methodology Used to Measure the Reported Benefit:

A judgmental sample of 974 Appeals, Collection, Examination, and Taxpayer Advocate office case files were reviewed at the Ogden and Fresno Service Centers and the Pacific-Northwest and Southwest Districts between January 2000 and March 2000. From this judgmental sample, we identified and confirmed with management that 96 case files contained ITP references after the RRA 98 was enacted.

From a November 1999 national computer extract of the ACS, we identified 1,850 case histories that contained key words (“ITP,” “TXPR,” and “PROTEST”) that could indicate an ITP reference. We reviewed a statistical random sample of 366 case histories and identified 89 (24.3 percent) case histories that contained ITP references. The sample is based on a population of 1,850, confidence level of 95 percent, precision of plus or minus 4 percent, and occurrence rate of 25 percent. Our sample size is valid to estimate over the population using our actual occurrence rate of 24.3 percent. Using this percentage, we estimate that approximately 450 of the 1,850 case histories contain ITP references.

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<sup>1</sup> Pub. L. No. 105-206, 112 Stat. 685.

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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### Finding and recommendation:

ITP coding remained on the Taxpayer Advocate Management Information System (TAMIS) and the Audit Information Management System (AIMS) (see page 7-8). This report recommends the removal and prevention of this ITP coding.

### Type of Outcome Measure:

Taxpayer Rights - Actual

### Value of the Benefit:

Two IRS computer inventory systems contained ITP coding on cases that were created after the effective date of the RRA 98 (176 records on the TAMIS and 83 records on the AIMS).

### Methodology Used to Measure the Reported Benefit:

From national computer extracts of the TAMIS and the AIMS taken between November 1999 and January 2000, we found cases that were identified as ITP coding for these systems, based on descriptions of coding in IRS management directives and program documentation.

### Finding and recommendation:

Operational manuals in different types of media still contain references to ITPs that could be inadvertently used by IRS employees (see page 9). This report recommends removal of ITP references upon the next revision of the operational manuals.

### Type of Outcome Measure:

Reliability of Information - Actual

### Value of the Benefit:

The IRS' Internal Revenue Manual (IRM) on different Intranet sites and in printed format contained ITP references that could be inadvertently used by IRS employees. One IRS Intranet site had ITP references in 134 sections of the IRM.

### Methodology Used to Measure the Reported Benefit:

In March 2000, we searched the IRM that is available to IRS employees on the IRS Intranet site called the Compliance Automated Research Tool System (CARTS). There were 134 ITP references in the IRM contained on the CARTS. A judgmental sample of 10 ITP references found on the CARTS was used to search the IRS Electronic Publishing Intranet site that contains electronic and printed versions of the IRM. In addition, the IRS Servicewide Electronic Research Project Intranet site was searched for ITP references in the IRM.

## **Additional Action Is Needed to Eliminate Illegal Tax Protester Designations**

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### Finding and recommendation:

Publications contain references to ITPs that could be inadvertently used by IRS employees (see page 11). This report recommends removal of ITP references upon the next revision of the operational manuals.

### Type of Outcome Measure:

Reliability of Information - Actual

### Value of the Benefit:

National IRS publications including letters, forms, documents, and training materials contained ITP references that could be inadvertently used by IRS employees. We identified ITP references in the titles of 15 publications; 10 of the 15 publications had been ordered after the effective date of the RRA 98.

### Methodology Used to Measure the Reported Benefit:

In September 1999, we searched the titles of IRS publications available to IRS employees on the IRS Electronic Publishing Intranet site. There were 43 publications with ITP references in the titles; however, 28 were labeled obsolete or were not a violation of the RRA 98. The remaining 15 publications with the ITP references were confirmed by the IRS Western Area Distribution Center in December 1999 as actively available for dissemination to employees. Using a Centralized Inventory Distribution System Transaction Report, we determined that employees ordered 10 of the 15 publications between November 1998 and November 1999.